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Dhafer, Omar

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# **Telecommunications regulation and the institutional foundation of the Palestinian Authority**

## **1. Introduction**

Telecommunications liberalisation has changed the rules of the game within the industry. One of the economic goals of liberalisation policy is to promote competition so that consumers enjoy better prices, quality and choice. Therefore, incumbent operators are no longer protected by exclusive and special rights. Abolishing exclusivities promotes market entry and competition, while enforcing asymmetric regulations to reach a level-playing field helps new entrants to compete with incumbent operators.

Liberalisation policies changed the rules of the game at the institutional level as well. The old model consisted of state monopoly supplying and regulating telecommunications. For liberalisation and competition to effectively work this model had to be modified and the state had to relinquish any vested interests in the market.

Another institutional change was the introduction of independent regulatory authorities. Although governments retained their right to set the sector's policy, the day-to-day management of the market became the responsibility of national regulatory authority. In some countries, such as Japan, South Korea, and Israel, regulation of the market remained the responsibility of the government.

This paper presents the case of the Palestinian Authority with regard to regulation of telecommunications and investigates its institutional foundation in order to decide on a compatible regulatory system. The paper follows a qualitative research approach in two parts. The first part examines the institutional endowment framework described by Levy and Spiller (Levy and Spiller, 1994; Levy and Spiller, 1996). It also presents comments and criticism of the framework and incorporates new developments on institutional capacity related to unstable states.

The second part presents the current institutional capacity of the Palestinian Authority and problems towards adopting regulatory reform and installing a better regulatory system that responds to the complex regulatory issues of today's telecommunications. Data was collected from governmental and international reports that track institutional developments in the Palestinian Authority and through interviews with key stakeholders in the Palestinian telecommunications sector <sup>[1]</sup>.

The remainder of this paper consists of the following: Section 2 provides a theoretical framework and examines Levy and Spiller's institutional endowment framework, section 3 presents a brief summary of the status of telecommunications in the Palestinian territories, section 4 presents Palestine's institutional endowment, section 5 discusses Palestinian Authority's fragility and its impact on regulatory reforms, while section 6 provides a brief conclusion.

## 2. Theoretical framework

### 2.1 *The regulatory state*

The debate on the need for regulation is deeply rooted in economics, political science and other fields. The free market school of thought, inspired by Adam Smith's invisible hand, argue that market forces can handle market inefficiencies without the need of the state's intervention through regulation. At the other extreme, the government intervention school of thought (public interest theory, capture theory, or economic theory of regulation) argues that market externalities justifies government intervention through regulation.

Hence, two competing approaches to regulation emerged (Lodge, 1999), the "Regulation as an act of benevolence" approach, which considers regulation as a necessity and the "Regulation as a conspiracy" approach, which considers regulation as a pure waste of resources. A third approach treats regulation as neither bad nor good but looks at regulation as a "question of design". This approach depends on agent-principal literature as it argues that best possible policy outcomes are produced if regulation is institutionalised and designed with a set of control mechanisms and defined processes for efficient, fair, accountable and transparent regulation.

Regulation by design was an essential component of telecommunications market liberalisation. Lodge (1999) argues that while the experience of European states differ, all states departed from the "welfare state" to the "regulatory state" as there was a shift from public ownership and economic stabilisation and redistribution policies towards procedural and performance-oriented regulation. Eyre and Sitter (1999) point out that regulatory reform has changed the institutional design and created independent agencies that embrace the principle of separation between operation and regulation. There were no more post, telegraph and telephone service agencies (PTTs) but independent national regulatory authorities (NRAs).

### 2.2 *State's institutional foundations*

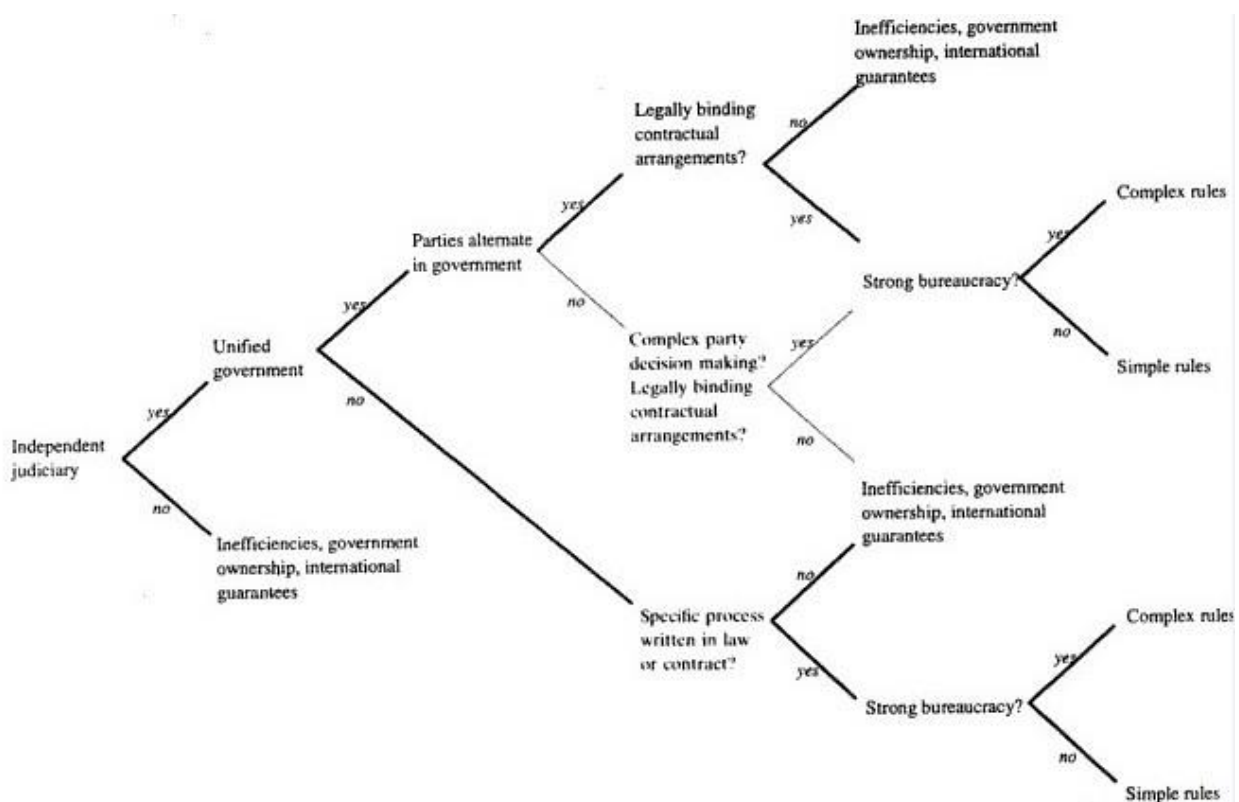
There is a vast literature on the institutional design of the regulatory process that covers issues related to a regulatory authority's structure, functions, procedures, and values<sup>[2]</sup>. There is also literature (eg Levy and Spiller, 1994; Levy and Spiller, 1996; Saleh, 2010; Stirton and Lodge, 2002; and Thatcher, 1999) that looks at regulatory reform and its relationship with the state's institutions. Since the objective of this paper is to identify the most compliant telecommunications regulatory system to be installed in the Palestinian Authority, it will discuss the later set of literature.

Levy and Spiller (1994, 1996) argue that the design of an effective regulatory system that ensures regulatory certainty and commitment depends on the country's institutional endowments. They look at regulation as a contract between a government and an operator and argue that because of the intrinsic characteristics of telecommunications (economies of scale, sunk costs, etc), governments have an incentive to attempt administrative exploitations in order to achieve short-term gains such as lowering local calls tariffs or setting better labour contracts. Their main focus was to study the formal and informal mechanisms that are embedded in the country's main institutions (judiciary, legislative and executive), which place formal and informal restraints on the government exploitation attempts, restraints on regulatory discretion, and constraints on

changing the regulatory system.

Development and enforcement of such restraining mechanisms depend on what they define as the country's institutional endowment (Levy and Spiller, 1994), which explains how laws and regulations are adopted and enforced (legislative and executive structure), how disputes are resolved (judicial system), the degree of influence social customs and norms have on adopting restraint mechanisms and the impact of state bureaucrats' experience on enforcing such mechanisms.

Such institutional endowment framework formulates a decision tree that defines the type of regulatory design compatible with the state's institutions. Figure 1 presents Levy and Spiller's decision tree.



**Figure 1. Levy and Spiller's regulatory design decision tree**

Using this decision tree, investors can decide whether to invest in a country that lacks an independent judiciary but has been committed to an international agreement, such as the World Trade Organisation's Basic Telecommunications Agreement (BTA), which would serve as an international guarantee that would protect their investment from arbitrary exploitation. On the other hand, a country would decide to efficiently use its resources and adopt a simple-rules regulatory system if it has a weak bureaucracy.

Therefore, regulatory design (governance and incentives) should be compliant with the country's

own institutional endowment. An unstable country, in that sense, may not be able to effectively import the telecommunications regulatory framework of a country like the UK, because it does not have the same institutional endowment of the UK in terms of an independent judiciary, a proper system of checks and balances, etc.

### 2.3 *Administrative exploitation or regulatory reform?*

According to Stirton and Lodge (2002) however, Levy and Spiller's model simplifies regulation into a one-dimensional contractual problem between the state and the operator(s). At the core of this problem is the assumption that governments' actions are nothing but attempts at administrative exploitation. Saleh (2010), Stirton and Lodge (2002), and Thatcher (1999) provide a different view.

Thatcher (1999, p. 8) explains that awareness of the possibility of competition has increased, especially after the deregulation movement in the USA and the UK during the 1980s. However, this political will of deregulation or liberalisation of the sector, led by the EU and national governments, was met with fierce opposition from the incumbent operators and labour trade unions.

Saleh (2010) explains in detail how globalisation has escalated the fight between new forces (global financial conglomerates, large manufacturers, retail chains<sup>[3]</sup>) pushing for the "flexible accumulation" model, which required opening up of the telecommunications sector to competition, and incumbent operators and trade unions fighting back to keep the Fordism model, which kept telecommunications under monopoly structure.

Stirton and Lodge (2002) argue that reducing regulation to a contractual problem<sup>[4]</sup> contributes to the premise that governments' behaviour is perceived as administrative exploitation rather than a genuine attempt to respond to economic developments (technological progress and its impact on the cost of supplying telecommunications services) and to ensure that regulations evolve to meet economic and social goals. In addition, the framework overlooks research in regulation regarding the capture theory, where network industries have been dominated by monopolies that have a high degree of influence on telecommunications-related policies.

Furthermore, Stirton and Lodge (2002) have examined the validity of Levy and Spiller's endowment framework on Jamaica by investigating empirical data on its regulatory system. They argue that the Jamaican experience on liberalisation provides a different explanation than the framework's initial hypothesis proposes. In particular, the fight between the Jamaican government and the private monopoly Cable & Wireless (C&W) on market restructuring does not present the hypothesis of a government trying to exploit private investment; instead, such a fight was essential for liberalisation of the sector, given that the government still honoured C&W's exclusivity agreement.

This explanation is interesting in two ways. First, it strengthens the validity of Levy and Spiller's framework as it proposes that Jamaica has been improving alongside the decision tree. Second, it calls to carefully read events of sectorial reforms in countries to determine whether such events

should be accounted as administrative exploitation or simply a part of normal conflict between political and economic agents until a new equilibrium is reached. Once a new equilibrium is reached and a new market structure is in place, the framework should be used to ensure that there is a match between a state's institutional foundations and its regulatory system.

Stirton and Lodge's (2002) validation of the framework and Favaro and Winter's (2004) account of institutional changes within Jamaica and the Eastern Caribbean states contributes to the conclusion that Jamaica's institutional endowment has changed and that by strengthening its capacity and achieving greater autonomy of its administration (both in telecommunications and in general) Jamaica's has climbed the ladder of Levy and Spiller's decision tree.

Other research contributes to the validity of the framework. For example, Bolhoff (2001, p. 16) studied institutional reform within the telecommunications industry in Germany and the UK. He found that the UK's initial regulatory design consisted of a regulatory agency (OFTEL) that had close links to the Office of Fair Trade (OFT) with regards to its design. OFTEL has a Director General with a degree of discretion as regulatory functions were assigned to the director general and not the regulatory agency, which is compliant with the British administrative tradition.

In Germany, Bolhoff (2001, p. 19) argues that although on a macro-organisational level, Germany was influenced by European law and the British model of a sector-specific regulatory agency<sup>[5]</sup>, traditional German administrative solutions influenced the organisation at the micro-level.

## 2.4 *Within the context of unstable states*

Smith (1997) explains that regulatory reforms are implemented in a smoother fashion within countries that have institutional experience in comparison to countries that do not. The issue of introducing effective regulatory systems in developing countries has been discussed within the context of developing countries' ability to institutionalise regulations despite corruption, inexperienced bureaucracy and unstable political systems.

Unstable states represent a subset of the developing states, where economic, social, and political problems are substantially more significant to their development. The term "Unstable State" includes a wide set of countries and is usually associated with the terms "Ineffective State", "Fragile State" and "Failing State" (Dhaher, 2011, p. 16). According to the OECD (2008), states are fragile "when state structures lack political will and/or capacity to provide the basic functions needed for poverty reduction, development and to safeguard the security and human rights of their populations".

Within the context of telecommunications fragility varies. Some fragile countries engaged in armed conflict experience insufficient and outdated infrastructures or a systematic destruction of infrastructure projects (Type A), while fragile countries that lack legitimacy or effectiveness experience weak and ineffective regulatory bodies (Type B). Other fragile countries would not have full control over the sector so that even if they have an efficient regulator, regulations are often not enforced (Type C). Dhaher (2011, p. 17) provides some examples of issues emerging



from fragile states, as shown below:

- Somalia (Type A): Six mobile operators, each covering a geographic region owing to civil war<sup>[6]</sup>.
- Arab countries (Type B): Absence of an adequate appeal process and ownership by ruling parties/family of telecommunications companies negatively affects quality of regulation (Sutherland, 2010).
- Kosovo (Type C): No international gateways are assigned to Kosovo. Regulatory authorities use Serbian and Slovenian international gateways (Cullen International, 2010).
- Palestinian territories (Type B & C): The bulk of core network (switches) are hosted outside the territory; spectrum frequency allocation is controlled by Israeli authorities; imported equipment takes a long time (years) for security clearance (World Bank, 2008).

Marshall and Cole's (2010) index of state fragility distinguish between fragility in government legitimacy and fragility in government effectiveness. Government legitimacy refers to the acceptance of political authority by population or political authority that is acquired or exercised according to certain socially accepted normative standards and criteria. Government effectiveness refers to the government's ability to capacity and institutional development.

Alemu and Khan (2011) show that inflow of direct investment funds depends on fragility in government effectiveness but not in government legitimacy. Investors seek to ensure that the government has put in place proper mechanisms to protect their investments and maintain rule of law. This finding explains why investments in telecommunications networks and services have been made in fragile states such as Egypt or Tunisia that lack government legitimacy but, nonetheless, have put in place some form of an effective institutional set up. It also supports Levy and Spiller's framework as it shows that the problem of regulation is actually a problem of commitment and effectiveness of the states' institutions.

Levy and Spiller (1994) investigated two fragile countries; Argentina and the Philippines. Their main findings show a political-investment cycle, where businesses that support one political party or social/ethnic group will be rewarded with high rents when the political party or social/ethnic group take power, while businesses that support their rivals will be deprived of any rewards. Corruption and low respect for the rule of the law were also observed in the two countries.

Problems of commitment and effectiveness can be solved when there is political will and capacity to install a legitimate and effective regulatory system. (Brown et al 2006, p. 85) The problem of low will and capacity can be expected in fragile states as governments resist attempts to reduce their control. In order to secure long terms in power, politicians will resort to illegal and economically damaging activities such as accepting bribes and other corrupt practices in exchange for the distribution of subsidies, licences, loans, jobs or services (Duckett, 2001, p. 23).

Within such an environment, an institutional vacuum can be expected, where impartiality of the

judiciary can be questioned, and control of the government over key decisions can be observed. The choices of the best regulatory system to choose from Levy and Spiller's decision tree will be confined to either state monopoly or a licence-based regulatory system with international guarantee.

### **3. Institutional foundations of the Palestinian Authority**

#### **3.1 *Brief summary of telecommunications in the Palestinian territories***

The economic annex of the declaration of principles agreement (Oslo agreement) in 1993 permitted the newly established Palestinian Authority to build and maintain public telecommunications networks in the Palestinian territories (West Bank and Gaza Strip). International gateways, spectrum frequency and equipment imports all remained under Israeli control and management. Disputes are resolved by the Joint Technical Committee, which consist of Palestinian and Israeli representatives.

The Ministry of Telecommunications and Post (later renamed as the Ministry of Telecommunications and Information Technology, MTIT) took charge of building a public telecommunications network in the West Bank and Gaza Strip. In April 1996, the 1996 Telecommunications Law was signed by the PA President<sup>[7]</sup>, which provided a legal and regulatory framework for the telecommunications and post sectors.

The law envisioned a typical model of a state-owned sector, where the ministry acts as both operator and regulator allowing, at the same time, private entities to get licences for either building public networks or providing value-added services. The goal of such a licensing regime is to create competition within the system. Licenses with monopoly clauses/status were considered illegal as indicated by article 7 of the law.

However, this vision changed rapidly. In the same year, the Ministry issued a 20-year licence for Paltel, a public shareholding company comprised of private Palestinian investors and the Palestinian Authority<sup>[8]</sup>, to build the network. The licence included an exclusivity period of 10 years for the fixed network and 5 years or 100,000 subscribers (whichever comes first) for the mobile network. The Ministry stopped supplying telecommunications services and resigned its role as sector regulator. Within two years, Paltel reached the 100,000 mobile subscribers threshold and, by the end of its exclusivity in 2006, it increased fixed lines penetration from 4% to 9%.

Market liberalisation efforts started in 2003. Three years later, Wataniya was awarded the 2<sup>nd</sup> mobile licence, 30% of which is owned by The Palestinian Authority owns through the Palestine Investment Fund. At the same time, a new telecommunications law that promotes market liberalisation and competition and introduces an independent regulatory authority was signed by the President. Nonetheless, the Palestinian Legislative Council rejected the law on two separate occasions. Therefore, the sector remained governed by the 1996 Telecommunications Law. Table 1 presents major events in market developments since establishment of the Palestinian Authority in 1994.



Year	Market developments
1994	Palestinian Authority is given the right to build public telecommunications network(s) in West Bank and Gaza
1995	Building and developing a national telecommunications network
1996	Paltel is awarded a 20-year wired and wireless telecommunications license to build, maintain, and develop the national telecommunications network. License included a 10-year exclusivity period for fixed telecommunication (ends in 2006) and a (5-year or 100,000 subscribers, whichever comes first) exclusivity period for mobile telecommunications. Ministry of Telecommunications and Post regulated Paltel's prices and quality.
2003	Calls for liberalisation of the market initiated by ISOC, Palestine Chapter, and the Palestinian IT Association of Companies (PITA) Paltel exclusivity on mobile ends (more than 100,000 subscribers)
2005	Paltel introduces the Subscription Free Internet initiative, using exclusivity clauses in its license. ISOC, PITA, and ISPs protest against it, but the Ministry approves it.
2006	Paltel exclusivity on fixed telecommunications ends. Ministry of Telecommunications and Information Technology issues a tender for a second mobile operator Wataniya, a Kuwaiti-based mobile operator is awarded a 3G mobile license. Wataniya Palestine is incorporated and started building its network. The legislative Council rejects the 2006 Telecommunications Law.
2007	Wataniya is denied spectrum by Israeli authorities. Operations are delayed.
2008	MTIT in West Bank issues licenses for broadband, VoIP, and Wi-Fi service providers. Wataniya awaits for Israeli authority to assign spectrum
2009	After diplomatic pressure, Israeli authorities agree to assign Wataniya 2G spectrum frequency in West Bank. Wataniya starts its commercial operations MTIT (West Bank) and Paltel sign an agreement that leads to Paltel's functional separation. Paltel is awarded a 3G mobile license, pending availability of spectrum. The 2009 Telecommunications law is signed by the president. The legislation committee of the paralyzed Legislative Council declares its intent to reject the law in the Council first meeting.
2010	MTIT (West Bank) introduces bitstream access as first step of introducing competition in data market. Same procedure is applied in Gaza by Hamas government.
2011	Israeli Authorities give Wataniya clearance to install base stations in Gaza and import and deploy needed equipment. A 2G service was scheduled to be launched around mid-2012.

**Table1: Governance and telecommunications development (1994-2011)**

### 3.2 *Institutional foundations of the Palestinian Authority*

The Palestinian Constitution<sup>[9]</sup> describes the governing system in Palestine as a parliamentary democratic system, where people directly elect their President and representatives to the Palestinian Legislative Council (PLC)<sup>[10]</sup>. The government is led by a prime minister (usually leader of the majority) appointed by the president and confirmed by the Legislative Council. A complete separation among executive legislative and the judiciary is maintained, while independence of the judiciary is emphasised. The economic system is based on free-market economy, where both private and public enterprises are allowed<sup>[11]</sup>.

The constitution sets up an institutional endowment that consists of an independent judiciary, a unified government with a possibility of parties alternating in government. Contractual

agreements are legally binding. The structure and organisation of institutions imply that constraints on governmental exploitation can be imposed and that regulatory system can be comprised of an institution that would be independent of the executive and accountable to either the legislative council or judiciary or both.

However, in reality the institutional endowment is contradictory to what has been described above. Using Levy and Spiller's framework, Palestine's institutional endowment resembles Argentina and the Philippines' institutional endowment, which is comprised of "Presidential rent-seeking" with a "political investment cycle." The following sub-sections provide a brief analysis of the judicial system, government and administrative capabilities of the Palestinian authority.

### **3.2.1 Judiciary**

There is almost no history of legal disputes related to telecommunications. A search of the Al-Muqtafi legal database<sup>[12]</sup> yields one<sup>[13]</sup> dispute between Paltel and the government (Ministry of Finance<sup>[14]</sup>). A major reason for that was the monopoly status of Paltel over the sector from 1996 to 2006 and the close relationship they enjoyed with the government, which reflects Levy and Spiller (1994) political-investment hypothesis.

Brown (2010) considers the judiciary system as weak and corrupt, and the World Bank<sup>[15]</sup> shows that control of corruption and respect of the rule of the law, which is one of the Palestinian High Judicial Council's<sup>[16]</sup> main elements of judicial independence, is low (less than 50 percentile). Interviewed stakeholders believe that independence of the judiciary is less of an issue compared to its capacity to resolve telecommunications and competition related disputes.

Unanimously, stakeholders argue that the qualifications and experience of judges to handle telecommunications cases and the speed with which a dispute is resolved carried more weight. For example, the Internet Society-Palestine (ISOC.PS) believes that the judiciary's independence is adequate, but its capacity to resolve telecommunications disputes constitutes a significant problem. For that reason, service level agreements (SLA) are common practice among telecommunications operators and service providers. SLAs act as a framework to resolve any future disputes and are considered by competitors as an additional guarantee on top of the ministry licences, which includes a list of duties, rights and forbidden (anti-competitive) practises.

This voluntary practise by the competitors and the compulsory licensing scheme by the ministry is compliant with Levy and Spiller's decision tree, where local (SLAs) and an international (World Bank supervised) licensing system is implemented.

### **3.2.2 Governing structure**

Except for a short period of time (2006-07), where Hamas emerged as a political rival, Fatah, the main political party in the Palestinian Authority, dominated the executive and legislative branches. Hence, the relationship between the legislator and the executive was smooth as the government had full discretion on social, economic and political issues and the legislative hardly

used its powers to enforce any type of restraint on government actions. With regard to telecommunications, a pattern of political-investment cycle (Levy and Spiller, 1994) can be observed on at least two occasions.

The first political-investment cycle started by the establishment of the Palestinian Authority in 1995 and lasted until 2006. While the 1996 Telecommunications Law envisioned a public network managed by the ministry and article 7 of the law prohibited any monopolistic activities, the government decided to award Paltel with an exclusive wired and wireless telecommunications licence. According to World Bank (2011), PA's decision to award Paltel with a statutory monopoly was sound and rational considering the high risk of operating in a politically unstable region. Nonetheless, this move by the government was a clear violation of the 1996 Telecommunication Law and met with no objections from the legislative council or any other institution.

Also, the World Bank (2011, p. 35) cites three violations within the licensing procedure that benefited Paltel. First, there was no formal public tendering process for the licence. Second, a licence was originally given to another group of investors but was revoked by the PA and given to Paltel. Finally, the licence and its annexes were kept confidential until 2008, when the licence, but not all annexes, was made public. Until that year, MTIT itself did not have a copy of the licence. In a recent interview, the current minister of telecommunications said that the ministry's efforts for increased liberalisation were constrained by Paltel's licence since some provisions are "above the law."<sup>[17]</sup>

The way the 1996 telecommunications provisions were ignored and Paltel's licence was handled shows that the government used its discretion to influence telecommunications-related decisions that favoured Paltel. Interested parties could not clearly identify and protest against some issues and MTIT and the government ignored any protests from the ICT stakeholders<sup>[18]</sup>.

The lack of formal attempts by the legislature or judiciary to impose any restraint on the government's decisions and the Palestinian Authority's shares in Paltel<sup>[19]</sup> are additional indicators of the close relationship between the government and Paltel.

The second investment cycle can be observed when a change in power occurred in 2005. As Fatah faced internal conflict, Mahmoud Abbas (a Fatah member) took power after the death of his political rival and the first president of the Palestinian Authority, Yasser Arafat.

A tender for a second mobile operator was issued and Wataniya, the Kuwaiti-based mobile operator, won the auction for a 3G mobile licence. Wataniya-Palestine was established. The Palestinian Authority, who sold most of its shares in Paltel, invested in 30% of Wataniya-Palestine's shares. Also, after it was awarded the licence, Wataniya-Palestine awarded an advertising company that is owned by the son of the Palestinian Authority President a major contract to run their promotional campaign across the West Bank<sup>[20]</sup>.

These two incidents accompanied by Paltel's low investments<sup>[21]</sup> and other governments'

attempts to liberalise the market show that the change at the political level has resulted in change of the businesses favoured by the government and enforces Levy and Spiller (1994, page 220) hypothesis that “business owners not aligned with the elite in power tend to be subject to administrative exploitation.”

### **3.2.3 Administrative capabilities**

Bureaucracy in the PA suffers from several inefficiencies that render its performance weak, such as a low level of expertise especially in policymaking and technical issues. Another source is corruption and weak enforcement of the law.

According to the MTIT’s deputy minister, the ministry offers around 10% of salaries offered by the private sector. This put an immense pressure on the ministry to attract skilled workers from an already small labour market and to keep up with market developments and complex regulatory tools<sup>22</sup>.

With regard to corruption, Transparency-Palestine<sup>[23]</sup> has issued several reports addressing corruption in the public sector. Also, the World Bank (2011) has published its report on enhancing governance and reducing corruption. Both organisations suggest that nepotism is the main source of corruption in the public sector.

Corruption and weak rule of law result in a process of selective enforcement, where some court orders are neglected, while others are enforced mainly because of political reasons. Violation of the rule of law is not uncommon. Within telecommunications, practices such as call tapping and website blocking are among the most common violations by security agencies. While such practices can be found in other countries, the real uncertainty comes from the fact that court orders specific to telecommunications disputes are overlooked by enforcement agencies.

## **4. The Palestinian Authority’s fragility and its impact on telecommunications regulations**

It is apparent that reality contradicts what was designed in the Palestinian constitution (2003). Table 2 provides a snapshot of the institutional foundations of the Palestinian authority. Applying Levy and Spiller’s decision tree to the Palestinian Authority, a licence-based system with international guarantees is the most adequate regulatory system that will match the Palestinian territories’s institutional foundations.

Legislative and Executive institutions	Judicial Institutions	Social Conflict	Social Norms	Administrative Capabilities
Separation of powers; Strong presidency; traditionally one strong ruling party with fragmented and weak	Weak and corrupt.	Regional competition with conflicting political agendas	Rent-seeking; lack of respect for rule of law	Weak and corrupt

opposition parties; unsuccessful alternating of power experience.				
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**Table 2:** Palestinian Authority Institutional Foundations

Nonetheless, policy makers are pushing for a more institutionalised regulatory system that implements a set of global best regulatory practices. For such a system to succeed, policy makers have to solve two serious problems that contribute to its fragility. Fragility has two main sources: endogenous, represented by its weak institutions, lack of respect for rule of law, and corruption; and exogenous, represented by Israeli control over vital telecommunications resources.

#### 4.1 *Endogenous fragility*

Assuming that the Jamaican scenario (Stirton and Lodge, 2002) is applicable to the institutional changes in the Palestinian territories, in the sense that a genuine attempt at regulatory reform is being led by the government, the resemblance ends here. This is because institutions in Jamaica have evolved (Stirton and Lodge, 2002), which merited them progressing on Levy and Spiller's decision tree. Therefore, the complex, rule-based regulatory system was not considered a mismatch with the country's institutional foundations. That is not the case for the Palestinian Authority as its attempt to install a complex-rule based regulatory system is crippled by the institutional foundations discussed in the previous section.

Despite many initiatives concentrating on building a “state of institutions<sup>[24]</sup>”, the process of building the states' capacity is slow and subject to many roadblocks. Within telecommunications, the past two ministers led most of the initiatives. However, institutionalising such activities is also moving at a slow pace. While the latest minister has brought in a qualified team that has better regulatory experience, the team is still crippled by the surrounding environment with many Fatah party conservatives still opposing reform<sup>[25]</sup>. The minister himself complained that, “the battle has not been won yet. Dark forces are still working hard.<sup>[26]</sup>” Interviewed stakeholders, in particular ISOC.PS, CoolNet and Mr Bahour, pointed to the ongoing struggle and inability of the ministry to institutionalise its activities creating a gap between individual and institutional know-how.

This failure of institutionalising regulatory reforms is an endogenous fragility that policy makers should address. Installing a sophisticated regulatory system is not a sign of institutional evolution but a mismatch that leads to wasted resources. One indicator of the institutional mismatch is the fact that operators and service providers put their trust in individual SLAs rather than the ministry's interconnection guidelines.

#### 4.2 *Exogenous fragility*

The International Telecommunication Union (ITU) accepted the Palestinian Authority as an observing member. This decision has two disadvantages. On the one hand, a full membership in the ITU and World Trade Organisation (WTO) would have placed an obligation on the Palestinian Authority to comply with international agreements and upgrade its institutional

foundations, which is similar to what Jamaica had done (Stirton and Lodge, 2002). On the other hand, full membership would have obliged Israel to adhere to ITU and WTO resolutions, thus creating more certainty in the market<sup>[27]</sup>.

Issues that remained under Israeli control were vital, most importantly, access to international destinations, importing of equipment, access to area C<sup>[28]</sup>, and frequency spectrum. Table 3 presents the problems and risks created by Israeli control and their impact on regulations and investment.

Issue	Description	Contribution to fragility
<b>International gateway access</b>	PA has its own international dialling code number (970), but does not have an independent international gateway, and is not permitted to use any international gateway other than the Israeli one, in effect, it doesn't matter for a caller in the US, for example, to use Palestine's (970) or Israeli (972) code to get through and connect to either a fixed or mobile Palestinian number.	<p>Inability to negotiate with neighbouring countries such as Jordan and Egypt for better prices for international traffic.</p> <p>Israeli operators have monopoly powers over Palestinian operators that result in higher cost for Palestinian operators and higher prices for consumers.</p>
<b>Importing equipment</b>	Over the last 15 years Palestinian operators suffered from Israeli authorities' continuous refusal to allow for some equipment to enter the Palestinian market.	<p>Networks are congested, at best, or poorly maintained and under-developed at worst.</p> <p>Paltel and Wataniya core network is hosted outside Palestine, which raise cost of supplying telecommunications service (Paltel main switches are hosted in London, England, which adds around US\$ 5 million to the cost of supplying telecommunications services. Likewise, Wataniya main switches are hosted in West Jerusalem.)</p>
<b>Access to area C</b>	Palestinian operators have to get authorisation from Israeli authorities to install its equipment in order to serve communities living there. Limited number of antennas installed in area C reduces availability and quality of mobile telecommunications.	<p>Low quality of telecommunications services.</p> <p>Loss of market share (20%-40%) to unlicensed Israeli mobile operators.</p>
<b>Spectrum frequency</b>	Managed by Israeli authorities. Israel delayed the release of spectrum allocated to Jawwal and Wataniya for 2 and 3 years, respectively.	Delayed operations, discouraged investors and decreased public trust in PA.

**Table 3:** problems and risk created by Israeli control on telecommunications resources and their impact on regulations and investment



While operators were able to overcome most of the above problems with good marketing strategies and product differentiation plans, the real problem is spectrum management. In both occasions, when the PA licensed Jawwal in 1997 and Wataniya in 2006, both companies had to wait for 2-3 years until Israel agreed to assign them spectrum<sup>[29]</sup>.

The case of Wataniya is interesting because only diplomatic pressure on Israel made it release the spectrum as Tony Blair used his diplomatic position as the Quartet's special envoy to pressure Israeli authorities into releasing frequencies<sup>[30]</sup>. Although denied by Blair, it seems that J.P.Morgan was behind such pressure as it was a shareholder of Qtel, the parent company of Wataniya. Another failing project was not an option for the troubled financial services giant<sup>[31]</sup>. Shortly after Blair's intervention, Israel released 2G frequencies and Wataniya started offering its services in the West Bank.

## **5. Addressing fragility and advancing through the decision tree**

Setting up a sophisticated telecommunications regulatory system requires the Palestinian Authority to address its endogenous and exogenous fragility. With regard to endogenous fragility, policy makers should realise that the regulatory state they are pushing for depends on procedural and performance-oriented regulations and expert and efficient bureaucracy (Lodge, 1999).

Thus, the Palestinian Authority has only one choice, which is to build its institutions and to train its bureaucracy. Until institutions develop, licence-based regulations are more adequate (Levy and Spiller, 1994). Operators and service providers can protect their investment through licences that clearly define the rights and obligations of each player in the market. The presence of the World Bank and the Palestinian Authority membership (albeit as an observer) in the ITU and WTO provide an international guarantee for businesses. In particular, the involvement of the World Bank as a close adviser to the ministry of telecommunications has helped to produce licences based on best international practices and to reassure investors that the Palestinian Authority is serious in its telecommunications regulatory reforms.

With regard to exogenous fragility, there is a need for other types of international guarantee that ensures Israel would comply and lift restrictions related to telecommunications. The most logical international guarantee would be the GATS' Basic Agreement on Telecommunications (BTA). The BTA could act as a framework that regulates Israeli-Palestinians telecommunications issues and provide an adequate conflict resolution mechanism. Since Israel is already a member of GATS, mode 3 of GATS' service delivery (Sinclair and Grieshaber-Otto, 2002) could be provoked and Israel would have to comply and lift any restrictions on the flow of foreign direct investment in the Palestinian territories including restrictions on spectrum frequency and equipment imports. However, in order to provoke mode 3 of GATS' service delivery, the Palestinian Authority must be recognised as a state, which renders GATS and BTA as non-enforceable.

The World Bank and USAID can play a role in enhancing Palestinian-Israeli relationship through

facilitating communication within the Joint Technical Committee<sup>[32]</sup>, but history shows that Israel has a bargaining power during negotiations and that implementation of decisions are frequently delayed.

Wataniya's spectrum case has shown that diplomatic pressure backed up by foreign investors might be a solution. This option, however, depends on the Palestinian Authority's ability to attract foreign investors to invest in its ICT sector. Since ICT-related foreign investments decisions are influenced by government effectiveness (Alemu and Khan, 2011), eliminating the Palestinian Authority's endogenous fragility becomes a prerequisite to eliminating its exogenous fragility.

## 6. Conclusion

This paper has presented the institutional foundations of the Palestinian Authority and explored the challenges facing policy makers in developing the Palestinian Authority institutions. It discussed two sources of fragilities that threaten regulatory reform and keeps Palestine's regulatory system confined to a basic licence-based system.

As most countries have entered the regulatory state, their respective appropriate regulatory system is a reflection of their institutional foundations. A mismatch between a states' regulatory system and its institutional endowment would not lead to desirable regulatory results, nor would it lead to regulatory certainty and the commitments investors seek to make investments in the states' ICT market.

A country's institutional foundations are represented by its judiciary, government and administrative capabilities, while social and political norms play an important role in building up those foundations and directing any subsequent reforms. Climbing up or down Levy and Spiller's decision tree depends on the state of the country's institutions.

Institutional foundations in fragile states are likely to consist of a weak and corrupt judiciary, an elite political group that monopolise the government without proper mechanisms of alternating the power within the country's social groups, and a weak, corrupt, and politically influenced bureaucracy. A political investment cycle that rewards businesses backing the elite political group in power and punishes other businesses backing rival political groups adds to the inefficiencies of the market, increases corruption, and decreases public trust in any regulatory system. For such environment, a license-based regulatory system backed with an international guarantee remains the most adequate to create minimum desired level of regulatory certainty and attract some investments to the market.

This paper has shown that Palestinian Authority's institutional foundations resemble those of fragile states. Its judiciary is weak, corrupt and too inexperienced to handle telecommunications-related disputes. Its governing system has been dominated for most of its lifetime by Fatah, and its bureaucracy is weak, corrupt and politically influenced. Two political investment cycles have seen businesses granted rents by the dominating political group, with the political group owning shares in these businesses.

Insisting on installing a sophisticated regulatory system is considered a mismatch with the Palestinian Authority's institutional foundations, which would lead to waste in resources and efforts. Instead, the Palestinian Authority should first develop its institutional foundations then its regulatory system will develop.

Nonetheless, the institutional development process is slow. Moreover, individualisation of institutional setup and internal conflict negatively affected institutional reform initiatives as it reduced them to a vision of few people who lack widespread support of the unskilled and politically influenced bureaucracy. This leads to effectiveness fragility in government, which negatively affects foreign investors' decision to invest in countries that have this type of fragility.

Exogenous fragility in terms of Israeli control over vital telecommunications resources, such as spectrum frequency, equipment imports, control over access to international destinations and service restrictions on area C territories within the West Bank is another factor affecting the Palestinian Authority's ability to effectively control its ICT market. As Palestine is not recognised as a sovereign state yet, international organisations' decisions, such as ITU and WTO, are not enforced.

The Wataniya spectrum frequency case gives hope to the Palestinian Authority that pressure on Israel can produce positive results. However, such pressure was a result of commercial lobbying. Flow of foreign direct investment (FDI) becomes a fundamental goal in the reform agenda. As FDI is influenced by government effectiveness and since the Palestinian Authority's endogenous fragility hinders its effectiveness, eliminating endogenous fragility becomes a prerequisite to eliminating exogenous fragility.

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<sup>1</sup> Interviewees consisted of a representative from: the Ministry of Telecommunications Information Technology; the incumbent operator (fixed, mobile, data) – Paltel; the second mobile operator – Wataniya Palestine; the Palestinian IT Association of Companies; the Internet Society, Palestine chapter – ISOC.PS; Mr. Sam Bahour, an expert involved in the regulatory process since 1996; and two representatives of newly licensed providers of broadband Internet, VoIP, and Wi-Fi.

<sup>2</sup> See Baldwin and Cave (1999), Geradin (2000), Geradin (2004), Smith (1997), Queck (2000), Stern and Cubin (2005), Stern and Holder (1999), and Stern and Trillas (2001)

<sup>3</sup> The common goal of the new forces is their desire to outsource part of their operations to countries around the globe. This process required constant communications. As international calls were expensive and well above their cost to subsidise the low cost of local calls, these forces demanded for competition in the telecommunications sector.

<sup>4</sup> The main objection here is that while such a narrow view would be true in developed countries, where social goals such as universal service and consumer protection could be attained if economic objectives are met (Nenova, 2007, p. 70), this is not the case in developed countries, where societal goals gain more importance and have more impact with regard to the trade-off between equity and efficiency.

<sup>5</sup> Thatcher (1999, p. 8) shows that European Law has helped European national governments to push for the desired structural reforms in the telecommunications sectors as governments argued that failure of implementation reforms



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is considered as a violation of EC rules.

<sup>6</sup> <http://developing-telecoms.blogspot.com/2009/07/somalia-while-daring-operators-turn.html>

<sup>7</sup> At that time, the Palestinian Legislative Council did not exist. Laws required signature of the PA President to be enacted.

<sup>8</sup> The PA has since sold most of its shares.

<sup>9</sup> <http://muqtafi.birzeit.edu/Legislation/PDFPre.aspx?Y=2003&ID=14138>. Arabic only, registration is required.

<sup>10</sup> Article 5 of the Constitution

<sup>11</sup> Ibid, Article 21

<sup>12</sup> [http://muqtafi.birzeit.edu/en/about\\_muqtafi.aspx](http://muqtafi.birzeit.edu/en/about_muqtafi.aspx) Al-Muqtafi stores all Palestinian legislation and courts' judgments since 1994. It archives all judgments and enacted laws, executive orders, and the constitution under the Palestinian Authority Jurisdiction.

<sup>13</sup> Few disputes between Paltel and citizens (subscribers or former employees) exist. The nature of such disputes ranges from use or sale of unlicensed equipment, payment of bills, and employment related issues. Though such disputes are out of the scope of this paper, courts have generally followed proper procedures and implied relevant law provisions in such cases. In cases where there was substantive error in judgment, appeal courts have corrected such mistakes. Therefore, it is safe to say that within ordinary company-citizen commercial disputes courts' judgments have been impartial.

<sup>14</sup> In its judgment, the Court of Appeal affirmed the decision of Court of First Instance that the dispute resolution body does not have the right to change or cancel any part of its decision and that by doing so its whole decision is annulled.

<sup>15</sup> [http://info.worldbank.org/governance/wgi/sc\\_country.asp](http://info.worldbank.org/governance/wgi/sc_country.asp)

<sup>16</sup> [http://pdf.usaid.gov/pdf\\_docs/PNADW388.pdf](http://pdf.usaid.gov/pdf_docs/PNADW388.pdf)

<sup>17</sup> <http://maannews.net/arb/ViewDetails.aspx?ID=410486>

<sup>18</sup> Perhaps the Subscription Free Internet initiative provides a clear example, where Paltel proposed a model that would effectively make it the only player in the wholesale market, while it would leave the retail market to Internet Service Providers. Despite protests from ISOC.PS, PITA, the ISPs, and others that such a move would effectively turn the competitive narrowband internet market (Broadband Internet was not available then) into a monopoly, where competing ISP would turn into resellers of Paltel's products, the ministry ignored such protests and approved Paltel's initiative.

<sup>19</sup> Over the years, the PA sold its share in Paltel. It currently hold a minority share of 6%

<sup>20</sup> <http://www.dailymail.co.uk/news/article-1311237/Special-investigation-How-Blair-rescued-Palestine-deal-worth-200m-2m-year-paymasters.html>. There has been misunderstanding of the role of the President's family with Wataniya. It was believed by many that the President's son owned shares in Wataniya.

<sup>21</sup> <http://maannews.net/arb/ViewDetails.aspx?ID=410486>. The current telecommunications Minister has declared recently that Paltel has to increase its investment, especially in NGN before both parties sit down for license extension negotiations in 2015

<sup>22</sup> For example, the ministry declared that cost of interconnection will be calculated using Long Run Incremental Cost method (LRIC) by April 2010. However, due to the lack of skilled employees on costing methods, LRIC estimations are not ready yet, and the ministry could not verify LRIC-based prices submitted by Paltel.

<sup>23</sup> <http://www.aman-palestine.org/eng/index.htm>. International Transparency's Corruption Perceptions Index does not include information on Palestine's public sector corruption.

<sup>24</sup> The latest initiative came from the Palestinian 13<sup>th</sup> government programme titled "Palestine: Ending the Occupation, Building the State" [http://www.mop.gov.ps/web\\_files/issues\\_file/090825%20Ending%20Occupation,%20Establishing%20the%20State%20-%20Program%20of%20the%2013%20government.pdf](http://www.mop.gov.ps/web_files/issues_file/090825%20Ending%20Occupation,%20Establishing%20the%20State%20-%20Program%20of%20the%2013%20government.pdf)

<sup>25</sup> Conflict among government agents was apparent during discussions of the 2009 Telecommunications Law that establishes the independent regulatory authority. The cabinet secretary was against the law as he declared during the discussions that "absolute independence would lead to tampering" and questioned the need for the law altogether. Also, the legislative committee of the Legislative Council declared its objection to the law.

<sup>26</sup> Correspondence via the IT Special Interest Group mailing list ([www.itsig.org](http://www.itsig.org)).

<sup>27</sup> In the case of Kosovo, which is not recognised as a sovereign state, the protection of the United Nations has

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helped in establishing communications networks and gaining international access through neighbouring countries (Cullen International, 2010). Without the protection of the United Nations, Israel has no legal obligation to adhere to international organisations' decisions such as the ITU and WTO.

<sup>28</sup> The Oslo agreement has split the West Bank and the Gaza Strip into three areas (A, B, and C). Area A includes territories that are under full authority (administration and security) of the PA. It mostly includes the main West Bank and Gaza Strip cities. Area B includes territories that are under partial authority (administrative), while security is controlled by Israeli security forces. It mostly includes towns near area A territories. Area C includes territories that are under the full authority of Israel. It mostly includes areas near borders, highways, and settlements. Territories in Areas B and C would eventually become part of Area A. In 2005, all of the Gaza Strip became part of area A, while most of the West Bank territories are either area B or C. The following map illustrates the situation in 2007. Nothing significant has happened since then.

[http://upload.wikimedia.org/wikipedia/commons/6/6a/West\\_Bank\\_%26\\_Gaza\\_Map\\_2007\\_%28Settlements%29.png](http://upload.wikimedia.org/wikipedia/commons/6/6a/West_Bank_%26_Gaza_Map_2007_%28Settlements%29.png)

<sup>29</sup> According to the Palestinian deputy ministry of telecommunications, spectrum frequency is a national security issue for Israelis. The decision to release more spectrum frequency is not taken solely by the Israeli ministry of telecommunications. According to *Haaretz* newspaper, Israel tried to convince Jawwal (Palestine) and Orange (Israel) operators to share some of its spectrum frequency with Wataniya in order not to release more spectrum frequency for commercial use. <http://www.haaretz.com/news/palestinians-still-waiting-for-better-cell-phone-service-but-is-it-israel-s-fault-1.279578>

<sup>30</sup> <http://www.jpost.com/MiddleEast/Article.aspx?id=187813>, see also footnote 25.

<sup>31</sup> In channel 4's *Dispatches* investigating programme, Peter Osborne investigates Blair's affairs in Middle East. With regard to the Palestinian territories, he shows that Blair, while employed as consultant to J.P.Morgan, used his diplomatic position as the Quartet's Special Envoy to pressure Israel into accepting spectrum release for Wataniya and the build of a gas field, in which J.P.Morgan has invested.

<sup>32</sup> The Joint Technical Committee was set up to overview implementation of telecommunications-related provisions of the Oslo agreement (World Bank, 2008, p. v).